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Agenda Item 4

November 15, 2011

TO: MEMBERS OF THE HEALTH BENEFITS COMMITTEE

I. SUBJECT: Long-Term Care Program 2011 Annual Valuation Report

II. PROGRAM: Long-Term Care

III. RECOMMENDATION: Staff recommends the Health Benefits Committee (HBC):

a. Approve the Long-Term Care (LTC) Program 2011 annual valuation report; and,
b. Lower the discount rate assumption from 7.79 percent to 6.25 percent for years 1-10 and 7.60 percent for years 11+ to reflect the recently adopted asset allocation.

IV. ANALYSIS:

The agenda item provides the HBC with the results of the CalPERS LTC Program annual valuation provided by United Health Actuarial Services, Inc. (UHAS) for the year ending June 30, 2011. This valuation provides a projection of future cash flows and evaluates the adequacy of current assets and premium levels based on those cash flows. The valuation utilizes a discount rate that reflects both the Portfolio 4 (P4) asset allocation adopted by the Board in May 2011, and the return expectations presented in March 2011 when the Board adopted the discount rate assumption for the Public Employees' Retirement Fund (PERF).

June 30, 2011, Annual Valuation Report

A valuation of current assets and premium levels was conducted by UHAS as well as an update of the projection of future cash flows.

Results of this annual valuation are based on the in force data and fund balance as of June 30, 2011. The results are expressed as a percentage of the present value of future net liabilities compared to future premiums. A positive percentage indicates the premiums are adequate to fund the future projected benefits.

Proposed Discount Rate

The P4 asset allocation adopted by the Board in May 2011 assumed a discount rate of 6.25 percent for years 1-10 and 7.60 percent for years 11+. A comparison of the current discount rate to the P4 discount rate and the resulting margins are provided in the table below.

To be consistent with the P4 asset allocation adopted by the Board in May 2011, and the approach used when setting the discount rate for the PERF in March 2011, we are recommending a more conservative discount rate than the current Board approved 7.79 percent. The proposed discount rate assumption reflects that investment returns from the P4 asset allocation are expected to be lower than historical returns over the next 10 years. It also reflects that investment returns for years 11 and beyond are expected to be higher than is expected of the next 10 years, but should be lower than the historical returns when looking back to the 1920s.

The proposed discount rates for the LTC Program for this annual valuation are:

- 6.25% for projection years 1 – 10 (fiscal year starting July 2011 to fiscal year ending in June 2021); and,
- 7.60% for projection years 11+ (fiscal year starting July 2021).

The following differences between CalPERS LTC Program and Pension programs are worth noting:

1. The LTC Program has a different proposed asset mix.
2. The LTC Program uses best-estimate (i.e., 50th percentile) returns for the discount rate and does not include provision for expenses or any margin in this rate. The LTC Program margin is explicitly provided for elsewhere.
3. The LTC Program is able to utilize a select-and-ultimate discount rate structure rather than develop one level discount rate required in the Pension valuations.

Key Findings

The following table compares the 2010 and 2011 annual valuation margin.

Valuation Date	Margin	Investment / Discount Rate
6/30/2010	24.25%	7.79%
6/30/2011	23.14%	6.25% years 1-10; 7.60% years 11+

It is important to note that the June 30, 2010, valuation margin of 24.25 percent was developed using the Board approved discount rate of 7.79 percent. The June 30, 2011, valuation margin of 23.14 percent was developed based on the proposed discount rate of 6.25 percent for years 1-10 and 7.60 percent for years 11+, that reflects the P4 asset allocation adopted by the Board in May 2011.

UHAS has assumed that on-going 5 percent increases would apply to policyholders owning LTC1 Lifetime plans with built-in inflation protection beginning in 2011. LTC1 Lifetime plans with built-in inflation protection represent 71,970, or 46.5 percent of our 154,634 policy holders as of June 30, 2011.

Cash flows during the period July 2010 to June 2011 exceeded expectations by $347.6 million mostly due to positive investment returns.

Funded Ratio

New for this valuation is a second method of expressing the current financial status of the LTC Program called a “funded ratio” which is consistent with the CalPERS pension and health plan financial status measurements. The funded ratio is the LTC Program assets divided by the accrued liability. In this context, a breakeven position is a funded ratio of 100 percent. The LTC Program’s funded ratio is 127 percent as of June 30, 2011. This ratio is based upon the Program assets as of June 30, 2011, and the discount rate of 6.25 percent for years 1-10 and 7.60 percent for years 11+.

V. RISKS:

If the recommendations are not approved, future Program valuations could lack accuracy by utilizing a discount rate that does not reflect both the P4 asset allocation adopted by the Board in May 2011, and the investment return expectations presented in March 2011, when the Board adopted the discount rate assumption for the PERF. As always, there is a risk of market fluctuations that could result in not achieving the new projected 6.25 percent investment return for FY 2011/2012.

VI. STRATEGIC PLAN:

This item relates to Strategic Goal X: Develop and administer quality, sustainable health benefit programs that are responsive to and valued by enrollees and employers.

VII. RESULTS/COSTS:

Costs associated are within the current terms of the agreement.

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ANN BOYNTON
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Benefit Programs Policy and Planning

Attachments